

Massive Influx Of Capital Boosts Prices For Power Plants

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In 2004, the private-equity firm U.S. Power Generating Co. had a tentative agreement to buy a power plant in Connecticut for \$220 million, but was ultimately elbowed aside by a group of hedge fund buyers.

Two years later, those funds sold the plant, known as Lake Road, for \$685 million to a European energy company.

The episode is indicative of the skyrocketing prices that firms are willing to pay for power plants and other electricity infrastructure, said Jay Worenklein, president of U.S. Power Generating Co, at a conference here hosted by Cambridge Energy Research Associates. This surge in prices has been fueled by a massive influx of capital seeking a home in power projects.

"You can't possibly overstate how liquid the sector is right now," Worenklein said.

"The amount of liquidity in the market is staggering," agreed Jeffrey Holzschuh, vice chairman at Morgan Stanley and head of the firm's power sector investment banking division.

Hedge funds are literally lining up to finance projects. When U.S. Power Generating Co. and several other firms spent \$950 million to buy three power plants in New York City, the number of funds who attempted to finance the acquisition far exceeded the number of investors who were finally let it on the deal, Worenklein said. Ultimately about 160 investors bought the project's debt.

"The debt financing is dominated by hedge funds," Worenklein said.

As states deregulated, utilities were forced to sell their power plants.

Following the collapse of power prices in 2001, the value of these assets dipped dramatically. But power prices have rebounded, as new power plant construction hasn't kept pace with rising electricity demand. The price of power plants has climbed steadily as well.

Hedge funds and private equity firms have shown an unflagging appetite for these assets. These firms can borrow money cheaply in today's low-interest rate environment for large power plant acquisitions financed mostly by debt.